

DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 04-0097
Sales/Use Tax
For the Year 2001

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ISSUE

I. Sales/Use Tax—Assessment on Purchase of Aircraft

Authority: IC 6-2.5-5-27; IC 6-8.1-5-1; 45 IAC 2.2-5-61;
Title 14 CFR, (Part) section 21, 43, 91, 121, 125, 135;
Panhandle Eastern Pipeline Company v. Dept. of Revenue, 741 N.E.2d 816
(Ind. Tax 2001); Cambria Iron Co., v. Union Trust Co., 154 Ind. 291, 55 N.E.
745 (1899);
Indiana Register, Volume 25, Number 7, April 1, 2002;
FAA AC 120-12A (4/24/86).

Taxpayer protests the assessment of sales tax on the purchase of an aircraft Taxpayer asserts is used in Public Transportation.

II. Sales/Use Tax—Trade in value of an aircraft

Authority: IC 6-8.1-5-1; IC 6-2.5-1-1; 45 IAC 2.2-3-6

Taxpayer protests the disallowance of the trade in value of an aircraft against the purchase cost of a new aircraft in determining the amount subject to sale/use tax.

STATEMENT OF FACTS

Taxpayer is a single member LLC disregarded for federal and state income tax purposes—consolidated with its owner, Parent. In March 2001, Taxpayer purchased an aircraft—a Raytheon Beechcraft King Air 350. Taxpayer was established with the intent to transport the employees, property, customers, and suppliers of Parent and Parent's affiliates. Taxpayer seeks the Public Transportation exemption to sales/use tax permitted in IC 6-2.5-5-27, which states:

Public transportation; acquisitions

Transactions involving tangible personal property and services are exempt from the state gross retail tax, if the person acquiring the property or service directly uses or consumes it in providing public transportation for persons or property.

The Department has promulgated a regulation addressing and defining Public Transportation, as it relates to the exemption. 45 IAC 2.2-5-61(b) states:

Definition: Public Transportation.

Public transportation shall mean and include the movement, transportation, or carrying of persons and/or property for consideration by a common carrier, contract carrier, household goods carrier, carriers of exempt commodities, and other specialized carriers performing public transportation service for compensation by highway, rail, air, or water, which carriers operate under authority issued by, or are specifically exempt by statute or regulation from economic regulation of, the public service commission of Indiana, the Interstate Commerce Commission, the aeronautics commission of Indiana, the U.S. Civil Aeronautics Board, the U.S. Department of Transportation, or the Federal Maritime Commissioner; however, the fact that a company possesses a permit or authority issued by the P.S.C.I., I.C.C., etc., does not of itself mean that such a company is engaged in public transportation unless it is in fact engaged in the transportation of persons or property for consideration as defined above.

Taxpayer owns the aircraft, and contracts with third parties for operation services and accounting services. Since the purchase of the aircraft, Third-party Operations has provided to Taxpayer travel related services—including pilots, maintenance, training, and assistance with certifications and warranties. Third-party Operations maintains Taxpayer's authority to operate under a Part 91 certification by the FAA. Third-party Operations initially provided to Taxpayer accounting services—including billing, check writing, and bookkeeping. In 2002, Third-party Accounting took over the accounting services previously provided to Taxpayer by Third-party Operations. Taxpayer, initially through Third-party Operations, and now through Third-party Accounting, bills Parent for the use of Taxpayer's aircraft by Parent's affiliates.

I. Sales/Use Tax—Assessment on Purchase of Aircraft

DISCUSSION

All tax assessments are presumed to be accurate. The taxpayer bears the burden of proving that an assessment is incorrect. IC 6-8.1-5-1(b). Tax exemption statutes are construed strictly in favor of taxation. Panhandle Eastern Pipeline Company v. Dept. of Revenue, 741 N.E.2d 816, 818 (Ind. Tax 2001). To prevail, a taxpayer must prove that it meets the requirements of IC 6-2.5-5-27. *See id.* Taxpayer asserts that it meets the statutory requirements of IC 6-2.5-5-27 for entitlement to the Public Transportation exemption. Taxpayer asserts it meets the regulatory requirements of 45 IAC 2.2-5-61(b) to be defined as a Public Transportation company. Taxpayer asserts it operates under 45 IAC 2.2-5-61(b) as a contract carrier.

Having received the evidence presented by Taxpayer and having considered the testimony given at hearing, the Department must apply the elements of the Public Transportation statute and regulation.

The Tax Court has stated that the public transportation exemption provided by IC 6-2.5-5-27 is an all-or-nothing exemption; if a taxpayer acquires tangible personal property for predominate use in providing public transportation for third parties, then it is entitled to the exemption, but if a taxpayer is not predominately engaged in transporting [third-parties or] the property of another, it is not entitled to the exemption. Panhandle, 741 N.E.2d at 819.

Public transportation of others is a serious matter—a high duty of care is imposed. Air travel is highly regulated. The Indiana Supreme Court—as well as courts across the land—have stated that a party cannot have the benefits without the burdens. See Cambria Iron Co., v. Union Trust Co., 154 Ind. 291, 301-02; 55 N.E. 745, 749 (1899). Taxpayer is seeking the benefits of the Public Transportation exemption—without assuming the burdens of being a Public Transportation entity. 45 IAC 2.2-5-61(b) states that public transportation carriers are required to operate under an authority—unless specifically exempted.

The aircraft is registered with the FAA to operate under Part 91 and is registered with the State of Indiana. Under the Department's Public Transportation regulation, an entity seeking the Public Transportation exemption is required to demonstrate that it is a public transportation entity by operating under the authority of—in this case—the U.S. Department of Transportation, specifically the FAA. While the regulation also mentions the Aeronautics Commission of Indiana, the agency has been subsumed into the Indiana Department of Transportation. Its primary function is the regulation and administration of airports. The *Indiana Register*, Volume 25, Number 7, April 1, 2002, p. 2206, states that the Aeronautics Commission of Indiana's rules are entirely repealed, transferred, or otherwise voided. The regulation also names the U.S. Civil Aeronautics Board. Taxpayer has not stated it operates as a Public Transportation entity under the authority of the Aeronautics Commissions of Indiana or the U.S. Civil Aeronautics Board. The Department mentions these two agencies so as to address those potential agencies that could possibly be invoked for qualifying for the Public Transportation exemption by operating under their authority. Taxpayer has stated that it operates as a Public Transportation entity only under the authority of the FAA. While Taxpayer is authorized to operate its aircraft—Taxpayer has not registered to operate its aircraft under FAA regulations as a Public Transportation entity. Taxpayer has not sought a Part 135, 121, or 125 registration with the FAA. These are public transportation registrations; they will be discussed further below.

The FAA has issued an Advisory Circular discussing private carriage versus common carriage of persons or property. FAA AC 120-12A (4/24/86). The FAA states that the advisory circular furnishes general guidelines for determining whether transportation operations constitute private or common carriage. *Id.* at 1. Operations that constitute common carriage are required to be conducted under Federal Aviation Regulations (FAR) Parts 121 or 135. Private carriage may be conducted under FAR Parts 125 or 91, Subpart D. Of note, the Department only permits the Public Transportation exemption for those operating under Part 125 if there exists a bona fide third party carriage operation. In Indiana, those operating under Part 125 in private carriage are not entitled to the Public Transportation exemption. An example of a bona fide Public Transportation exemption under Part 125 is where a professional sports team has a contract with an air carrier to transport the team. This is a contract carrier. An aircraft is dedicated to transporting the team; the general public cannot obtain a ticket. But the aircraft is owned and operated by a bona fide third party. The professional sports team has secured exclusive rights to use that aircraft. Lest Taxpayer attempt to argue that it is structured similarly to this, it needs to be noted that these professional sports teams have secured the exclusive right to fly on an airliner aircraft. Airliner aircraft are held to stricter safety and operation standards. An airliner aircraft cannot be operated under Part 91; they must operate under the safety and operation requirements of an airliner; they are held to the requirements of transporting the public. It is this combination of heightened regulatory standards and a bona fide contract to carry a third party that qualifies a taxpayer in Indiana to secure the Public Transportation exemption under Part 125.

Concerning operating as a Public Transportation Company under the authority of the FAA—Taxpayer is registered with the FAA under Part 91 instead of Part 135. The significance of this difference requires an explanation of FAA registration regulations. All aircraft are required to possess an airworthiness certificate—an FAA document which grants authorization to operate an aircraft in flight. There are two different classifications of FAA airworthiness certificates: FAA Form 8100-2, **Standard Airworthiness Certificate**, and FAA Form 8130-7, **Special Airworthiness Certificate**. Title 14 CFR, section 21.175 (FAR Part 21.175) defines the two different classifications of airworthiness certificates. Standard Airworthiness Certificates are airworthiness certificates issued for aircraft types certificated in the normal, utility, acrobatic, commuter, or transport category, and for manned free balloons, and for aircraft designated by the FAA Administrator as special classes of aircraft. Taxpayer's aircraft qualifies under this. Special Airworthiness Certificates are restricted, limited, and provisional airworthiness certificates, special flight permits, and experimental certificates. A Special Airworthiness Certificate is issued to aircraft not meeting the requirements for a standard airworthiness certificate. This LOF only will address Standard Airworthiness Certificates—because the Special Airworthiness Certificates are beyond the scope of concern for this LOF. An airworthiness certificate is transferred with the aircraft. FAR Part 21.179. Standard airworthiness certificates are effective as long as the aircraft is registered in the United States and the maintenance, preventive maintenance, and alterations are performed in accordance with FAR Part 43 and FAR Part 91. FAR Part 21.181.

Under Standard Airworthiness Certificates, a registered owner or an owner's agent of an aircraft applies for particular operation certificates. These commonly are referred to as (FAR) Part Registrations. There are four Part Registrations:

Part 91—**Private Carriers**

General Operating and Flight Rules

Part 121—**Airline Operators**

Air Carriers and Commercial Operators

Part 125—**Business and Commercial Airlines**

Airplanes having a Seating Capacity of 20 or more passengers or a maximum payload capacity of 6,000 pounds or more

Part 135—**Air Taxi Operators**

Commuter and On-Demand Operations

As can be seen, Parts 121, 125, and 135 are operation certificates for airlines, commercial operators, commuter, and on-demand (charter) services. These are Public Transportation operations—the systematic transportation of others (persons and property). Parts 121, 125, and 135 are classified under Subchapter G of Title 14. Subchapter G is entitled, **Air Carriers and Operators for Compensation or Hire: Certification and Operations**. Those operating under these Parts need to acquire a Part 119 Air Carriers and Commercial Operations Certification. Part 91 is classified under Subchapter F, entitled, **Air Traffic and General Operating Rules**.

The baseline registration is a Part 91 registration. All owners and aircraft are required to adhere to these general operating and flight rules—as well as the basic pilot and maintenance requirements. Specific types of aircraft and business operations are required to obtain more stringent Part Registrations and to operate under more demanding regulations. For example, under a Part 91 registration, any qualified pilot may fly an aircraft—regardless of age. But under a Part 121 registration, a pilot may no longer fly an airline aircraft after age 60—because of safety and operation concerns. There are five pilot certificates (licenses) granted by the FAA:

1. A **student pilot certificate** (license) is designed for the initial training period of flying. The student pilot must have a flight instructor present. He or she can solo after appropriate instructor endorsements.
2. A **recreational pilot certificate** limits the holder to: specific categories and classes of aircraft, the number of passengers which may be carried, the distance that may be flown from the departure point, flight into controlled airports, and other limitations.
3. A **private pilot certificate** lets the pilot carry passengers and provides for limited business use of an airplane.
4. A **commercial pilot certificate** lets the pilot conduct some operations for compensation and hire.
5. An **airline transport pilot certificate** is required to fly as captain by some air transport operations.

The FAA regulations require that a pilot operating under a Part 135 air carrier certificate hold a commercial pilot license—with a minimum of 1200 hours of experience as a pilot-in-command. FAR Part 135.243(c)(2). Some operations are required to have a flight crew of at-least two pilots. FAR Part 135.4. This LOF focuses on the requirements for a Part 135 because Taxpayer owns and operates a Raytheon Beechcraft King Air 350 with the potential to seat from nine to fifteen passengers. Taxpayer has configured its aircraft to accommodate eleven passengers, plus a pilot and co-pilot seat. Such an aircraft best qualifies to operate commercial and public transportation services under a Part 135—instead of a Part 121 or Part 125—since the aircraft is not a commercial airliner. Operations under Part 135 are designed for smaller commercially operated aircraft.

Under a Part 135, those engaged in commuter or air-taxi operations are held to higher safety and operation standards than Part 91. FAR Part 135.141 prescribes the additional aircraft and equipment requirements for operations as an air carrier. Some of the heightened requirements apply only to certain aircraft or passenger numbers, but all demonstrate heightened regulation of those being carried in public transportation.

Taxpayer stated at the protest hearing that Third-party Operations maintains Taxpayer's aircraft according to Part 135 requirements. There is no requirement under Part 91 that the aircraft be maintained and operated according to Part 135 requirements. Taxpayer voluntarily chooses to do so. Taxpayer could choose in the future to maintain the aircraft merely to Part 91 requirements. Certification to operate under Part 135 as an air carrier would ensure that Taxpayer—consistently and without waiver—is mandated to the standards of a Public Transportation entity. With a Part 135 Registration, Taxpayer would be operating under FAA authority as a Public Transportation entity—as required under 45 IAC 2.2-5-61(b). Also note that Taxpayer stated only the aircraft is maintained to Part 135 standards; Taxpayer did not state that the aircraft is operated according to Part 135 requirements. Because Taxpayer has configured the plane to seat eleven passengers, certain heightened safety and operations regulations are triggered under Part 135. There are additional requirements for air carriers when they transport nine or more passengers. Because Taxpayer's aircraft is registered under Part 91, these additional measures are not triggered as mandatory requirements; Taxpayer voluntarily can choose to adopt and adhere to them, but it is not held to the mandatory requirements by any authority to which it has submitted itself.

Taxpayer seeks the benefits of the Public Transportation exemption without the burdens of public transportation regulations. The Department requires those seeking the Public Transportation exemption to act as a public transportation entity—subject to the stringent

regulations of Part 135 (or Part 121, Part 125). Taxpayer operates under Part 91—a less stringent set of regulations. If Taxpayer seeks the Public Transportation exemption—then Taxpayer is required to seek authority to do so and must submit and operate as required by that authority. That means Taxpayer be registered and operate under Part 135, not Part 91.

Taxpayer asserts it purchased the aircraft for the purpose of engaging in Public Transportation. Concerning Taxpayer's assertion that it is a Public Transportation entity, this introduces evidence of Taxpayer's intentions when it registered the aircraft with the State of Indiana. In March 2001, Taxpayer filed a Form 7695, **Application for Aircraft registration or Exemption**. The registration process is similar to the registration of a motor vehicle—legal registration occurs and a concurrent assessment of sales/use tax is made. On the form, Taxpayer in Section D, **Sales/Use Tax Information**, checked the box to claim a tax exemption, choosing **Rental or Lease to others**. A cross check of the merchant number shows a filed Form ST-105, **General Sales Tax Exemption Certificate**, in which Taxpayer has checked off to indicate a **Single Purchase** for the aircraft as a **Sale to Retailer, Wholesaler or Manufacturer for Resale Only**. Taxpayer held out at the time of registration that it was purchasing the aircraft for rental or leasing to others. Taxpayer now seeks the Public Transportation exemption. The Department is confused by Taxpayer's assertion that Taxpayer purchased the aircraft for the purpose of engaging in Public Transportation—since it originally filed an exemption for rental and leasing. Accepting the premise that Taxpayer decided to reclassify the exemption to which it is entitled, if Taxpayer genuinely seeks to hold itself out as a public transportation entity, it would have filed with the Department to amend Form 7695.

Two years later in September 2003, the Department requested that Taxpayer provide documentation to substantiate the Purchase for Resale exemption. The Department asked to be provided flight schedules and logs, the entities leasing the aircraft, and a copy of the rental and lease agreements. Taxpayer indicates that it received the letter in the wrong department and because of this unintentional failure to provide information, the use tax assessment was triggered. The fact exists that Taxpayer now is arguing it is entitled to the Public Transportation exemption—not purchase for resale for rental and leasing—but the registration has not been amended to indicate this intention. Form 7695 requires that a taxpayer seeking the Public Transportation exemption indicate under what FAA Part the taxpayer is operating the aircraft. The taxpayer also is required to submit a copy of the FAA Certificate for Public Transportation. This would be evidence of an authority to be classified and operate as a public transportation entity. The FAA Certificate for Public Transportation is a document issued by the FAA permitting an aircraft to be operated in the public transportation of others. Taxpayer has not submitted a Part 121, Part 125, or Part 135 Certificate for Public Transportation. Common sense indicates that it is a Part 135 Public Transportation Certificate that is due to the Department—given that Taxpayer's aircraft is not a large airliner, but a small aircraft with a maximum passenger capacity of fifteen. Taxpayer may submit an FAA Certificate for Public Transportation under Part 121, Part 125, or Part 135. The Department merely is exercising common sense as to which Part Certificate it likely should expect from Taxpayer.

Taxpayer is entitled to amend Form 7695, **Application for Aircraft Registration or Exemption**. However, the September 2003 letter sent by the Department seeking documentation to substantiate Taxpayer's claim for exemption is the focal point at this time. Evidence was presented at the hearing in an attempt to substantiate an exemption under Public Transportation. But Taxpayer has not submitted any evidence of an attempt to amend Form 7695 to indicate its change in the basis of its exemption status. An attempt to amend Form 7695 would be strong

evidence to indicate the intentions of Taxpayer's exempt claim. That and the submission of an Air Carrier Certificate. As it currently stands, Taxpayer is arguing the Public Transportation exemption without having amended Form 7695 and submitting the requisite documentation to accompany the registration. Based on Form 7695, Taxpayer still is seeking a tax exemption for Rental or Lease. Since no evidence has been submitted to substantiate renting or leasing to others, and since Taxpayer did not present this argument at the hearing, the exemption is denied on this basis. Taxpayer has based its tax protest on seeking the Public Transportation exemption. The Department wishes to foreclose Taxpayer from coming back later to try a second time under another exemption provision. The Department will not be caught between conflicting positions. Taxpayer brought forward its protest under Public Transportation—so this is the one to which Taxpayer is held.

Directly addressing the Public Transportation exemption, Taxpayer has not provided the requisite documentation to indicate that it operates as a Public Transportation entity. To have done, so Taxpayer would have needed to have amended Form 7695. Overlooking this—for the sake of discussion—Taxpayer still would need to submit documentation that it is operating as a Public Transportation entity. That requires submitting to the Department a copy of an FAA Certificate for Public Transportation. Taxpayer argues that the statutes and regulations permit it to operate under Part 91. This is unconvincing. As discussed in length and detail above, the FAA has stringent requirements regarding the registration and operation of aircraft for hire. Taxpayer cannot glean the benefits of the Public Transportation tax exemption without also assuming the regulatory burdens of being a Public Transportation entity. Taxpayer is not operating under the authority of the FAA as a Public Transportation entity.

I. Sales/Use Tax—Assessment on Purchase of Aircraft

FINDING

For the reasons named above, Taxpayer's claim for the Public Transportation exemption is denied. Additionally, a future attempt to claim under the Rental and Sales exemption is denied.

II. Sales/Use Tax—Trade in value of an aircraft

DISCUSSION

All tax assessments are presumed to be accurate. The taxpayer bears the burden of proving that an assessment is incorrect. IC 6-8.1-5-1(b). Taxpayer purchased its aircraft from an Indiana dealer. Every aircraft dealer making a sale of an aircraft required to be licensed in the State of Indiana must complete a Form ST-108AC and must send the original to the Department. Form ST-108AC is a summary of the transaction and requires that a description of the aircraft purchased and any aircraft traded in. Then there is a computation for the amount subject to sales or use tax.

The dealer entered the selling price of the aircraft purchased as \$5,138,292.00. Where the trade-in allowance should be entered, the area has been stricken with a stripe of correction fluid. This means that no trade-in allowance has been entered. Taxpayer seeks to be able to subtract \$825,000 for the trade-in allowance. IC 6-2.5-1-1 permits a like kind exchange of personal property. However, the persons exchanging the property must own the property prior to the exchange. Implicit in the meaning of the word **exchange** is a contemporaneous transfer to each

other. *Webster's Third New International Dictionary* includes in the definition of exchange, "the process of reciprocal transfer of ownership." For a sale to have occurred, a contract must exist. That means that all bargaining has been completed. Because all bargaining has been completed, it is understood that each party understands what has been offered and accepted.

For this reason, at the time of the sale, the dealer would have known the agreed trade-in value of the aircraft being exchanged. That agreed price would be listed on Form ST-108AC. The trade-in allowance amount listed is blank, but more importantly—whatever had been placed in the space for the trade-in allowance amount has been stricken with a stripe of correction fluid.

45 IAC 2.2-3-6 states that only the trade-in value of an aircraft for another aircraft may be deducted from the selling price for sales [and use] tax purposes. The Department will grant the trade-in allowance amount listed on the original ST-108AC. That amount is blank. An attempt to amend the trade-in allowance amount after the fact does not comport with the intention of the like kind exchange—which is a contemporaneous transfer. Form 7695, **Application for Aircraft Registration or Exemption**, also has a stripe of correction fluid in Section D where the trade-in allowance is to be placed—which would reduce the amount subject to sales and use tax. Taxpayer's attempt to seek \$825,000 as the trade-in allowance is disallowed because the indicia of reliability as to that amount is suspect. Without speculating as to why the amount of the trade-in allowance has been stricken and left blank, the Department looks to the amount listed by the dealer on Form ST-108AC. That amount is blank.

II. Sales/Use Tax—Trade in value of an aircraft

FINDING

The taxpayer is sustained on the amount listed on the ST-108AC and denied the \$825,000 trade-in allowance sought.